

## Canopus Managing Agents - Syndicate 4444

### **Financial Strength Rating**

None

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**RatingsDirect  
Publication Date**

Feb. 5, 2010

Editor's Note

### ***Lloyd's Syndicate Assessment***

3-/Stable

### ***Financial Strength Ratings And Lloyd's Syndicate Assessments***

Standard & Poor's Ratings Services' insurer financial strength rating on Lloyd's (the Market; A+/Stable) remains the primary indicator of the level of financial security afforded to a policyholder of any syndicate trading in the Market. Lloyd's Syndicate Assessments evaluate, on a scale of '1' (very high dependency) to '5' (very low dependency), the extent of a given syndicate's dependence on the Market rating.

### ***Major Assessment Factors***

#### ***Strengths:***

- Good competitive position
- Good operating performance
- Conservative investment strategy

#### ***Weaknesses:***

- Limited financial flexibility available to Canopus
- Exposure to potential large losses

### ***Rationale***

The Lloyd's Syndicate Assessment (LSA) on Canopus Managing Agents - Syndicate 4444 (Canopus or Syndicate 4444) reflects its good competitive position, good earnings, and conservative investment strategy. The assessment is constrained by the limited financial flexibility, and the syndicate's exposure to large loss events.

The syndicate's competitive position is good, based on its size (£550 million capacity for 2010) and well-diversified underwriting portfolio. In addition, the syndicate has a good lead position in many of its key lines, and strong renewal business retention.

Standard & Poor's Ratings Services considers Syndicate 4444's operating performance to be good. While the syndicate performance has typically underperformed the Lloyd's average in recent years, it demonstrates lower volatility than some peers. The result for 2008 was affected by hurricane and risk losses, demonstrated by a published combined ratio of 104% (this includes 5 percentage points of foreign exchange gains). The consistency of the syndicate's performance is demonstrated by its five-year average combined ratio of 101%, including the catastrophe-affected years of 2005 and 2004; the standard deviation is low at 6.4. Net income for 2008 was strong, as a result of a strong investment return for the year. We expect underwriting performance for 2009 to show a significant improvement.

The syndicate has a conservative investment portfolio, which has generated consistently good returns to partially offset previous underwriting losses, and to enhance the performance in 2008. Most invested assets are held in highly-rated, fixed-income investments, with more than 70% being rated 'AAA', or are cash deposits with highly-rated institutions. The syndicate has a small amount of exposure to higher-yielding assets.

Canopus Group Ltd.'s (CGL) principal financial backer is Englefield Capital, a private equity firm. The total amount Englefield has invested in CGL exceeds its normal single investment limit, and its earliest investment in Canopus is approaching the typical average maturity of such a fund, so we believe that there is limited prospect of additional investment from the majority shareholder. Financial flexibility is therefore somewhat constrained. However, we acknowledge Englefield's consistent track record in supporting Canopus' growth with additional capital when required, and willingness to fund future growth at the syndicate, as seen at the start of 2008.

In addition, the syndicate writes a material amount of catastrophe-affected business. While historical catastrophe losses have been in line with peers and not material in the context of Canopus' overall capitalization, there remains the potential for a peak loss to cause a reduction in capital adequacy. This concern is partially allayed by the syndicate's strong catastrophe risk controls.

### ***Outlook***

The stable outlook reflects Standard & Poor's expectation that the syndicate's operating performance will improve in 2009, and that the syndicate's diversification and risk profile will make it less volatile than many of its Lloyd's peers. In addition, we expect the syndicate's competitive position to remain good, and the capital adequacy of the group to remain supportive of the current assessment.

Operating performance for 2009 is expected to show a significant improvement on 2008, partly because of recent rate rises but primarily because of a more-benign claims environment, particularly for catastrophic and large risk claims. The combined ratio for 2009 is likely to be around 90%. The syndicate will benefit in 2010 as the recent rate rises are earned through. We expect its enterprise risk

management program to continue to improve operating performance, particularly by controlling underwriting risk.

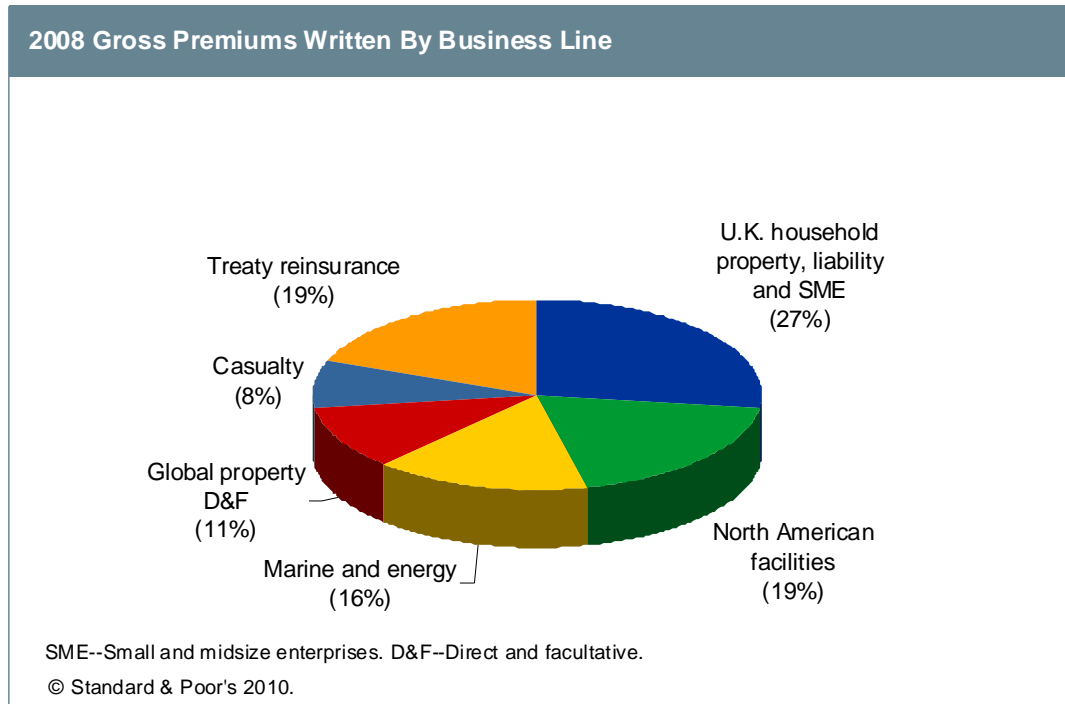
Syndicate 4444's competitive position will remain good, with the syndicate continuing to develop its diverse portfolio. We expect premiums to increase significantly by around 50%. Much of this will relate to foreign exchange movements; the underlying premium increase is likely to be around 15%. The syndicate will continue to develop its newer platforms, expanding as competition allows. The restructuring of the group's distribution capability in the U.K. presents a longer-term opportunity for the syndicate.

The outlook may be revised to negative if the syndicate fails to generate consistent underwriting profits, or strategic or operational developments result in constrained capital adequacy at the group level. Upside potential in the assessment would depend on the syndicate demonstrating the robustness of its competitive position through generating underwriting and bottom-line performance in line with similarly assessed peers.

***Syndicate Profile: Midsize Syndicate, Focusing On Short-Tail Risks***

Syndicate 4444 began trading at Lloyd's for the 2004 underwriting year, having been created from a management buyout of the operations of the Trenwick-managed syndicate 0839, which ceased business in 2003. It is managed by Canopus Managing Agents Ltd. (CMA), a wholly owned subsidiary of Canopus Holdings UK Ltd. (Canopus Holdings), which is itself a subsidiary of CGL. During 2006, the group acquired Creechurch Holdings Ltd. Former Creechurch syndicates 1607 and 3786 no longer write business and were reinsured to close into Syndicate 4444 in 2009. The managing agent also managed the life Syndicate 44; this was sold during 2008. For 2008, the group assumed the reinsurance to close of Syndicate 0839's 2001 and prior years of account. The group's non-Lloyd's activities include Canopus Ireland, which writes a small number of structured transactions into the group's class 3A Bermuda reinsurer on a collateralized basis. Syndicate 4444 accounts for around 95% of the group's written premium.

Syndicate 4444 writes a diverse account, with a focus on short-tail direct risks (see chart for the split of gross premium written in 2008). Around three-quarters of the syndicate's book is short tail, and about 75% is direct insurance.



***Competitive Position: Good, Based On Size And Diversified Offering***

Within the Lloyd’s context, Syndicate 4444 has a good competitive position, based on its size (£550 million capacity for 2010, ranking in the top quartile at Lloyd’s by capacity) and well-diversified underwriting portfolio.

The syndicate’s competitive position reflects the good spread of risks underwritten. In addition, it has demonstrated the strength of its position through good renewal retention in recent years, and has the capacity and willingness to lead business. The syndicate’s position has developed through the successful acquisition, integration, and retention of Creechurch and ongoing developments to acquire new underwriters in new areas. Together, these factors have developed the size and scope of the Canopus offering. The syndicate has developed new platforms to access business, for example in Singapore and Bermuda; however, these operations are still in their formative stages and the syndicate lags some more established Lloyd’s groups in its ability to access business through nontraditional channels.

The syndicate’s competitive position is enhanced by its expanding distribution platforms. In addition to sourcing business through traditional Lloyd’s brokers, the group has acquired or developed various other distribution capabilities. With the Creechurch acquisition, the group acquired two U.K.-focused service companies, Impact and Charrington, which offer accident and health, professional indemnity, and general liability business into the syndicate. These have been merged and renamed Canopus Underwriting Ltd.; developing this distribution capability remains a focus for the syndicate.

The group also has two underwriting agencies; Arista and Canopus Underwriting Bermuda Ltd. Arista, a joint venture with Equity Insurance (not rated), sources business from U.K. small and midsize enterprises through a network of regional offices. Growth in this entity was slower than initial management expectations, reflecting the very competitive nature of this market. However, Arista represents a long-term opportunity to establish a regional distribution capability in lines integral to the syndicate; the U.K. represents the syndicate’s second-largest market. In 2008, the group established

Canopus Underwriting Bermuda Ltd., a managing general agency writing excess casualty and treaty reinsurance business for Syndicate 4444. Again, the managing general agency (MGA) has written below its initial budget, reflecting the pricing environment in its key lines. More recently, growth at both these entities has been stronger.

The syndicate has also opportunistically expanded into new lines where appropriate underwriting resource is available, and which fit into the syndicate strategy. Examples of this are the direct engineering book started in 2010, and the crisis-management account developed in 2008.

Canopus continues to focus on expanding its book when and where market conditions allow. We expect it to grow if market conditions improve, but in the short term the extent of its growth will depend on rate adequacy and the company's acquisition and recruitment policies.

### ***Management And Corporate Strategy: Focus On Developing Business Through Managing Cycle And Diversifying Distribution And Product Offering***

Canopus' management team is considered a supporting factor for the assessment, having effectively managed the various strategic developments made by the group in the past few years. The successful integration of Creechurch, additional equity raising, and acceptance of the reinsurance to close of Syndicate 0839 reflect positively on our view of management.

Management aims to increase the syndicate's scale and diversity while remaining committed to bottom-line profitability. As the pricing environment remains difficult, management's focus is on profitably developing and enhancing the distribution and underwriting capabilities at the syndicate, while taking advantage of opportunities should they arise.

The main strategic goals of the syndicate remain unchanged. Management has focused on developing an underwriting franchise at Lloyd's. Most of the business remains short-tail insurance, but the syndicate is willing to write longer-tail and reinsurance business at a sizeable level if market conditions are suitable; as technical rates remain strong in catastrophe-exposed reinsurance lines, the syndicate will increase its exposure to catastrophe covers. Action take to build new operations, such as Canopus Underwriting Bermuda Ltd. and those in Singapore, will create the infrastructure to scale up operations as rates improve. Standard & Poor's considers management to be risk-aware and have a rational, achievable strategy for targeted, profitable expansion.

### ***Operational management***

The syndicate is managed along traditional divisional lines, with the group underwriting director responsible for all underwriting departments. The underwriting reporting line is to the agency underwriting director, with all other functions reporting to the chief operating officer.

During 2009 the agency CEO retired, and has been replaced on an interim basis by the group CEO; a permanent replacement is expected during 2010. The departure does not negatively influence Standard & Poor's view of the management team due to the depth of management resources at the syndicate and group. The syndicate is also aware of potential forthcoming retirements, and has succession plans in place for these.

Developing the syndicate's underwriting performance to a level commensurate with more highly assessed peers would be integral to positive assessment movement; previous investment in management and risk systems should leave the syndicate well-placed to do this.

***Financial management***

The company's individual capital assessment process has resulted in investment in risk modeling capability. The syndicate allocates capacity by line of business, although with a qualitative overlay focusing on rate adequacy. Canopus monitors and forecasts risk pricing by line of business and sets minimum required pricing, regardless of the competitive environment. The syndicate's focus is on underwriting risk; investment risk is low (see "Investments" below) and financial risk at the group level is acceptable.

***Enterprise Risk Management: Adequate With Strong Risk Controls***

Enterprise risk management (ERM) is viewed as adequate with strong risk controls. The syndicate has strong control processes for all its major risks, namely underwriting (pricing and reserving) and catastrophe risks. Standard & Poor's considers ERM to be of moderate importance to its assessment, given the company's potential exposure to large losses and the number of disparate types of insurance written.

Underwriting risk controls are considered strong. Underwriting risk is controlled through the use of clear limits for underwriters, which are linked to the underwriting policies and procedures and the individual divisions' risk registers. All risks are peer-reviewed, and an additional level of expert review exists to enhance controls over underwriting. The syndicate uses an exception reporting system to flag any potential issues. Weekly meetings between the divisional underwriters ensure controls are consistently applied throughout the syndicate. Other underwriting risks, such as those coming from delegated authorities, are controlled through an internal audit process. Reserving risk is controlled through quarterly review of reserve adequacy, the results of which are discussed through regular meetings of the reserving committee. Catastrophic risks are controlled through the use of aggregate monitoring across business lines and the integration of catastrophe modeling expertise in the underwriting process.

The syndicate has a developing, but as yet unseasoned, strategic risk management framework. The continued development of the individual capital assessment model has allowed the syndicate to align the business planning process with its capital requirements and costs. However, business decisions are not yet based on risk-reward trade-offs based on the capital modeling process. The syndicate is working on upgrading its modeling capability to integrate it into the day-to-day decision-making process. This could be a trigger for upward movement in the ERM assessment, as well as performing a key role for the implementation of Solvency 2.

***Accounting: Capital Based On Group Financials***

Capital adequacy analysis for the syndicate is based on the financial resources of the ultimate holding company, CGL. For 2007, the group adopted International Financial Reporting Standards (IFRS) for the first time. The result was an increase of £6 million in net assets, primarily as a result of immediate recognition of negative goodwill arising from the Creechurch acquisition.

***Operating Performance: 2008 Affected By Large Losses, But Historic Performance Good Overall, And Less Volatile Than Peers***

The syndicate's operating performance has been good, although the 2008 year was affected by a number of large losses. The combined ratio for 2008 deteriorated to 104% (this includes 5 percentage

points of foreign exchange gains) from 97% in the prior year. This reflected increased claims frequency and severity, and in particular net losses of \$45 million arising from hurricane Ike. This result is slightly behind peers, and lags the Lloyd's market as a whole. However, the syndicate's operating performance history over a longer period is good, and has demonstrated lower volatility than many Lloyd's peers. This is demonstrated by a five-year average combined ratio of 100% and the low standard deviation of 6%. This reflects the less-volatile nature of the business underwritten by the syndicate, compared with many Lloyd's peers, in particular the U.K. homeowners' and North American facilities books, which are some of the syndicate's largest.

Profitability is expected to improve in 2009, reflecting a benign claims environment, both through the absence of U.S. hurricane loss activity and a reduction in large property risk losses. As such, we expect the syndicate to produce a combined ratio in the low 90s for 2009. In 2010, the syndicate will benefit from rate rises achieved during the year as these are earned through. A positive investment result will lead to a good bottom-line result for the syndicate.

The increasingly competitive market had put the syndicate's operating performance under pressure, especially using a combined ratio metric, due to the syndicate's high cost base. Successful cycle management remains the key factor for the syndicate's longer-term profitability.

### ***Investments And Liquidity: Conservative Investment Strategy Supported By Strong Credit Quality***

The investment portfolio is strong and highly liquid. This reflects Lloyd's membership requirements for funds to be readily liquid and placed in low-risk investments—typically highly-rated bonds and international bank deposits.

As at Dec. 31, 2008, the syndicate's investment portfolio consisted primarily of fixed-income securities and cash, with a modest exposure to hedge funds. This allocation of investments reduces potential volatility in investment income. The credit quality of fixed-income investments was very strong, with all the syndicate's fixed-income holdings being at least investment-grade, and over 65% being rated 'AAA'. This conservative asset allocation philosophy produced a positive return in 2008, and will likely generate a positive result in 2009. Given the reduction in yields on the types of asset the syndicate currently holds, the syndicate is willing to take increased credit and duration risk going forward; however, Standard & Poor's believes that the investment allocation will remain conservative in the medium term.

The syndicate does not strictly match the duration of its assets to that of its liabilities, but the current maturity duration of its investments, about 2.5 years, is consistent with the predominantly short-tail risks underwritten.

### ***Capitalization: Retained Earnings Support Capital Adequacy***

Overall capitalization is considered good, supported by CGL's good capital adequacy. The additional capital injection of £59.2 million from the majority owner in February 2008, and the continued retention of profits supports capital adequacy. About 15% of the syndicate's capacity still comes through quota-share reinsurance support, although this amount has decreased and Canopus believes it could support 100% of the syndicate capacity.

**Reserves**

Reserving appears good. The loss-settlement trends by continuing lines of business have generally positive results, increasing our confidence in Canopus' reserving techniques. Independent actuarial review also attests to the sufficiency of the syndicate's reserves. Reserves for major events have typically been stable; although there was some deterioration in 2005 from losses arising from hurricane Wilma, initial loss reserves for hurricane Ike have improved. Some benefit is likely to accrue from the syndicate bringing its reserving function in-house during 2008.

**Reinsurance**

The overall level of underwriting risk protection afforded to the syndicate by its reinsurance program is good, reflecting a highly diversified and strong security rating structure. Canopus' strategy is to underwrite for gross profit. The reinsurance program is therefore designed to provide protection from extreme events by each line of business, and was effective in minimizing the syndicate's 2008 hurricane losses and flood losses in 2007. The program is heavily weighted toward nonproportional excess-of-loss covers.

The largest single-event exposure for the syndicate is a Gulf of Mexico windstorm, with net exposure to such an event estimated at around 15% of Canopus' 2009 capacity, well below the 20% ceiling set by Lloyd's, and containable within current capital adequacy.

**Credit quality**

The credit quality of the syndicate's reinsurance counterparties is strong. In 2009, most program participants were rated in the 'A' category or above by Standard & Poor's.

**Financial Flexibility: Constrained By Dependence On Private Equity Ownership**

Canopus is largely funded by venture capital provided by Englefield to CGL. The likely medium-term nature of Englefield's investment in CGL is mitigated by its consistent track record in supporting Canopus' growth with additional capital when required, and willingness to fund future growth at the syndicate, as seen at the start of 2008. However, the syndicate remains dependent on Englefield for additional funding, if required.

<i>Canopus Managing Agents - Syndicate 4444/Financial Statistics</i>					
	<i>—Year ended Dec.31—</i>				
<i>(%)</i>	<i>2008</i>	<i>2007</i>	<i>2006</i>	<i>2005</i>	<i>2004</i>
Combined ratio	103.8	93.2	92.9	107.5	105.1
Loss ratio	65.8	51.4	61.2	69.2	68.5
Expense ratio	38.0	41.8	33.5	38.3	36.6
Return on revenue	(0.2)	10.2	8.0	(5.6)	(4.3)
Premium retention ratio	85.1	85.7	92.3	84.6	91.2
Loss retention ratio	89.3	81.3	180.0	70.1	85.4
Reserves/net premiums written	143.7	112.3	88.7	95.7	60.6
Receivables ratio	26.0	30.8	34.4	43.3	54.8
Liquidity ratio	79.8	78.0	69.0	43.1	38.8

<b>Ratings Detail (As Of 05-Feb-2010)*</b>	
Canopus Managing Agents - Syndicate 4444	
<b>Holding Company</b>	Canopus Group Ltd.
<b>Domicile</b>	United Kingdom

\*Unless otherwise noted, all ratings in this report are global scale ratings. Standard & Poor's credit ratings on the global scale are comparable across countries. Standard & Poor's credit ratings on a national scale are relative to obligors or obligations within that specific country.

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